

## **THE FUTURE OF BUSINESS ETHICS? Legal Regulation, Ethical Standard Setting and Institutional Design**

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Business ethics futures is a new area of speculative investment that has yet to establish a track record. They are not yet listed on the Chicago (or Sydney) Futures Exchange and no one has yet suggested that such a listing would be anywhere as successful as the high flying pork bellies of the early 1980s.<sup>1</sup> Nevertheless, financial writers and commentators are continually talking about them and predicting as big a future for ethics as they once predicted for the likes of Alan Bond and Christopher Skase. Some Vice Chancellors and research granting bodies are investing in ethics futures and there are many people who are prepared to pay to be told about ethics (and a much larger number who are prepared to pay even more to be told that they are already ethical). At times some may wonder whether ethics will take over business in the 90s or whether ethics will be taken over by the business practices of the 80s.

The authors are not inclined to the pessimistic tone of the first paragraph. In particular, it is not the purpose of this article to suggest that some universities which like to see themselves as becoming more 'business-like' are becoming more like the businesses of the 1980s. This paper will however ask some questions about business ethics as it stands today and the different answers which could suggest different futures for business ethics. We will suggest our preferred answers to some of them and the way we should go about answering others. In this way we hope to make a tentative suggestion for the path that business ethics might take in the future.

The questions we will pose are as follows:

Why is there so much interest in, and apparent commitment to, business ethics?

- is it just advertising?
- is it to ward off legal regulation?
- is it to re-establish traditional economic centres of power?
- is it merely long term self interest?
- is it to make our lives more morally valuable?

What form should business ethics take? Should it be:

- an aspirational code?
- an enforceable code?
- the positive morality of business?

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<sup>1</sup> It is remarkable that although a flying pig is considered a wondrous thing, the markets of the 1980s had little difficulty in getting bellies of pigs off the ground in a big way by merely imagining, and trading, them before they were detached from the pig and sent to market! It was, of course, merely the first of the gravity defying efforts of the 1980s financial imagination!

- the critical morality of business?
- From where should it spring?
- management fiat?
  - ethical circles?

What role should business ethics play?

- Can it operate independently or must it operate in conjunction with other measures to improve the conduct of business?

While these answers are not mutually exclusive, we will suggest that the future of business ethics should lie in emphasising the last answers to each question. Business ethics should be firmly based on other-regarding values. The critical morality of business should be the centre of debate over business ethics. And business ethics cannot be expected to shoulder the burden of improving business conduct alone. It is the major thesis of this paper that, like many other problems of the late twentieth century, the problems of business conduct can only be addressed by a combination of legal regulation, ethical standard setting and institutional design. We will argue that the key to achieving co-ordination between the three is to look to the justification of modern business and use the values thereby exposed to provide the values around which ethical standards may be proposed and argued, the main source of the purposes for which laws are framed and by which they are interpreted, and the functions to which the design of institutions should be dedicated.

### **Why is everyone talking about business ethics?:**

There are several reasons for today's widespread interest in, and discussion of, business ethics.

For some it is just a matter of advertising or window dressing. Given the grave concerns raised about the conduct of business, talking about ethics may make consumers, customers and shareholders happier to deal with particular companies and their boards.

For others business ethics may appear as a way of warding off legal regulation. Much of business activity was deregulated in the early to mid 1980s and various disasters followed. The correlation between the deregulation of the banking system and the massive asset speculation hardly needs to be restated. This might imply that a degree of re-regulation is necessary and that other proposals for deregulation should be seriously reconsidered. Yet many still appear wedded to deregulation either because of ideological conviction or because deregulation has effectively transferred power to themselves. This latter point should not be forgotten. The removal of government regulation does not lead to the disappearance of the power formerly exercised by the government. It merely redistributes it to others.<sup>2</sup> This can be benign when ordinary individuals benefit in largely equal measure. It is a cause for concern if that power is redistributed to the already powerful.<sup>3</sup>

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<sup>2</sup> Sampford used to call it the 'privatisation of power', until he concluded that public/private distinctions were more often misleading than helpful.

<sup>3</sup> See Sampford, C., 'Law, Institutions and the Public/Private Divide',

Accordingly, the emphasis on ethical rather than regulatory solutions protects private power from threatened government limitation. However, we wonder if it may also subconsciously attract some as a way of regaining or redistributing private power. We have heard some analyses by senior business people that the problems all lie in the sharp practices of some of the new money. For them the solution lies in rediscovering the 'traditional values' of earlier days. When we have heard this story in Melbourne the problem has been given a geographical location and a political affiliation, the allegation being that the Labor government had a hatred of the Melbourne business establishment and hence favoured the new boys from Sydney who would take them on. Establishing and policing codes of ethics is a method of effectively excluding undesirables - but one must always be aware that business people may be undesirable to others for a variety of reasons and only some of those reasons are a matter of ethics.<sup>4</sup>

We do not raise these more questionable motivations in order to undermine the efforts of those who are seeking to improve the conduct of business in Australia by talking about business ethics. Indeed our paper and the National Institute's 'Law, Ethics and Business' project is predicated on the feasibility and utility of such efforts. However, it is important to appreciate that such motivations as the above are likely to be the prime motivations for some and a subsidiary motivation for others and they are part of the reason for the current prominence given to business ethics. While we are arguing for business ethics as a matter of principle others are using ethics as an expedient device for the pursuit of narrowly defined economic self interest.

For most of those involved in the discussion and promotion of business ethics the above considerations are supplementary if considered at all. Most would support business ethics either on the basis that it is in the long term interests of market players to act ethically or that there are independent reasons to act ethically based on the moral worth of the relevant conduct. These two arguments may be mutually supportive in most cases, but there the division is fundamental. Even where the long term interest argument is used as a supplementary argument there is a real danger. While it is true that this argument will stiffen the resolve of those who would act ethically it opens the way for the players to see some exception to the rule. The danger is that it encourages business people to retain their belief that their sole duty is to maximise profits and subsume ethical imperatives under that value. This would encourage them to adopt unethical behaviour when it does appear to be more profitable in the long term. While the fate of some of the sharpest and least ethical business people of the 1980s remains a fresh corporate memory this is less likely to occur. However, we should not forget that a statement that ethical practice is in a business person's self interest would have been

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Forthcoming (1991) *Federal Law Review* .

<sup>4</sup> This should serve as a reminder that 'self regulation' is something of a misnomer. The regulation is generally done by some body with the power to positively or negatively affect the interests of the relevant profession/industry and their clients/customers. The mere fact that it is not governmental power should not blind anyone to the fact that it is a form of power.

very dubiously received in the early 1980s and could again be weak in the late 1990s. It may be that current perceptions of the dangers of unethical behaviour are sustained<sup>5</sup>; it may be that business people will henceforth find that the calculus of long term self interest always comes out in favour of ethical behaviour; it may be that business people could be persuaded to exclude arguments that unethical practice is profitable in the long term as either too difficult or too tempting<sup>6</sup>. But it is more likely that ethical practice and long term self interest can clash at times. We must insist that the prescriptions of ethics would take precedence in such conditions.

If long term arguments are introduced, we would not want them confined to arguments of self-interest but used to emphasise other-regarding and deontological ethical argument. We could remind business with the Keynes' line that 'in the long term we are all dead'. This leads those of religious bent to suggest that, in the long term, they have to face judgment. Others might point out that if you live your life only for yourself, all your ends and purposes die with you: but that if you live your life in part for ends outside yourself then those ends may continue, giving a kind of immortality.

Whatever the arguments adopted, it is important that the arguments of self interest are supplementary rather than dominant. Ethics cannot survive as a contingent outcome of an entirely selfish consequentialist calculus<sup>7</sup>.

### **What form should business ethics take?:**

Before considering the content of business ethics and the ways in which we may seek to provide that content there is a more basic question as to the form business ethics should take. There are essentially four models involving two types of code and two types of morality.

The medical and legal professions provide examples of written ethical codes and many see business ethics as requiring a similar written code. Those codes can be divided into disciplinary codes that set the lowest common denominator of conduct and aspirational codes which set out the highest standards to which all should strive. Those who fall below that minimum standard of the disciplinary code are punished. The same cannot be true of aspirational codes as anyone who fell short of the best would have to be punished.

Those in favour of disciplinary codes point to the ability to sanction offenders while not intruding onto the individual's moral space. The concern is expressed that we should not police what people think - merely what they do.

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<sup>5</sup> Something that is unlikely because the phenomenon on which it depends - the sight of unethical business people continuing to get their comeuppance - would require that significant numbers of business people are unpersuaded of it.

<sup>6</sup> Raz argues that a practical reasoner may exclude snap judgements based on apparent short term profits because of the possible damage to long term gains. See Raz, J., *Practical Reason and Norms*, London, Hutchinson, 1975

<sup>7</sup> This is not to say that forms of consequentialism (e.g. classic utilitarianism) cannot ground some extremely strong ethical principles - but only by the essential, and extremely difficult, move of valuing the interests of all persons equally.

We should have clear rules and sanctions for unacceptable behaviour but beyond that people should be free to do as they please lest we fall subject to a tyranny of the moral majority. This is essentially a liberal argument in favour of law against the enforcement of morality and rests uneasily with the idea of having business ethics at all. To a large extent it merely turns ethics into a form of legal regulation where the rules are made by business (although the sanctions will frequently have teeth provided by the general law). This will make it possible for those who make the regulations to know their subject better and for those regulated to make a greater commitment to the standards. But it may also lead to the kind of white-washing of which some professional bodies are accused. More fundamentally, a disciplinary code focuses on the lowest common denominator beyond which business may feel it should not bother to go. It also concentrates on the unethical actions that should be avoided rather than the positive ends that should be sought. Finally, it encourages concentration on the text of the code and legalistic arguments that the relevant action does not fall within the prohibition. This is not to say that such rules do not have a place.<sup>8</sup> However, we would treat such enforceable codes of conduct as a form of legal regulation and would make of them the same point as we would of more standard forms of law - that they are only really effective if backed up by internalised ethical values.

The need for such values lead some to prefer the positive or critical morality models of business ethics (with aspirational codes having a role in moulding such morality). Of these, most are likely to emphasise positive morality - the current standards of conduct which business consider to be appropriate. There are two problems with such an emphasis. First of all, there is the difficulty of determining which group's positive morality should be so privileged - that of business as a whole, the industry (e.g. used car dealers?), or the firm (e.g. Quintex?). Secondly, there is the difficulty of determining what values are actually shared. Finally, and most importantly, tying business ethics to the relevant positive morality provides no room for those who would criticize current values and re-enforces the claims of a moral majority in business.

This brings us to the last alternative - of treating business ethics as a matter of critical morality in which individuals can debate, discuss and criticize majority views, internalising their own values and acting on them. Because these values are those of the relevant individuals they can be adopted whole-heartedly and given their full value. For the same reason there can be no moral tyranny. And there can be no danger of legalism (if you avoid your own values the first person you cheat is yourself and, unless you are dishonest with yourself the transgression is immediately known).

The usual objection is that this approach will lead to chaos with everyone pursuing their own conflicting view of the good. If you are not tied to common values (be they the common values of positive morality or those incorporated in law) then any action can be justified. Whereas in the past you

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<sup>8</sup> Nor does it prevent both aspirational and disciplinary codes being applied simultaneously, or even appearing in the same document. However, it is important to clearly distinguish which rules perform which functions.

had to hire a lawyer to get around an inconvenient law and argue that your action was legal, you would be able to hire a philosopher to get around an inconvenient moral principle and justify your action as moral. Given the current job market for philosophers and their inexperience of the commercial world this would almost certainly be cheaper.

While having no wish to dampen the job prospects for philosophers (even for the benefit of lawyers!), we believe that the objection is not well founded. The answer lies in the relatively public nature of the critical morality suggested. We want to encourage discussion about actions by business people among themselves so that they can form their own prior views of what principles should guide their lives. Some of these discussions would be by senior business people on a national scale. But most of them would be discussions by small groups of business people from the same firm or the same industry so that they could work their way through real and hypothetical problems. The role played by these groups could be seen as analogous to that played by 'quality circles'. They could even be called 'ethical circles' which would harness the same energies and dynamics that can be used to improve the quality of the corporation's output (although the nature, size and operation of these groups would vary considerably with the nature of the enterprise). In this case the idea would be to harness the experience and the ideals of the workforce to make the institution a more ethical place that lives up to the values which justify it. In these groups, employees could discuss ethical issues to develop their own critical morality and move towards a shared morality.<sup>9</sup>

In these circles, the emphasis should not be on *ex post facto* rationalisation but on debate, discussion, and the prior commitment to public positions on how executives and employees should behave. Discussions of this kind tend to produce a degree of convergence in opinion and, where there are differences, for differences to be known.<sup>10</sup> If executives are known not to support a particular value or feel constrained by a particular moral prohibition, their action will cause no surprise and, in many cases, less damage. Such discussions will lead to a greater degree of knowledge and self-knowledge and a genuine commitment to the values expressed and the likelihood of severe criticism for failure to live up to stated principles.

While we have a clear preference for emphasising business ethics as critical morality, it is perfectly possible, and generally desirable, to pursue more than one approach at a time provided that the functions of each are recognized. Aspirational codes can help raise the standards of behaviour. Disciplinary codes can be an important part of the way that corporations run themselves - although they should be recognized as essentially a part of law rather than

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<sup>9</sup> It is no coincidence that this approach to business ethics treats employees more like professionals. Neither is it a coincidence that it treats employees as having values to contribute in the same way as more modern management practices recognize employee contributions in terms of knowledge and skill.

<sup>10</sup> They also serve to sort out some of the conflicts and convergences between critical morality and the positive morality of the community, the industry and the firm.

morality. However, we would argue that critical business ethics should provide the impetus and the critical and self-critical questioning for this activity. Indeed, the kind of critical morality we suggest should assist in improving the positive morality of business and can provide a more visionary element for aspirational codes and detailed discussion that can assist in the drafting of in-house codes.

**From where should it spring?:**

It should be noted that this kind of ethics is very decidedly bottom up rather than top down. For some, business ethics is seen as another management tool and ethical codes are developed by management, perhaps with an input from outsiders. The code may even be written into the terms of the employee's contract.

This kind of business ethics is treated with a good deal of cynicism. There can be a perception that it is trotted out by the management every time something goes wrong and can be seen as an implication that the ethical problems of the business are the problems of the staff whereas many members of staff will, rightly or wrongly, see the root of the ethical problems in senior management. Certainly that was the complaint of several employees of both government and non-government corporations at a recent public seminar conducted by the Queensland Electoral and Administrative Reform Commission.<sup>11</sup> The ethical circles suggested above would raise ethical problems in the context and at the level at which they arise and would not only contribute to the development of a critical morality by individuals but would provide valuable inputs into codes of ethics that are more likely to be supported and acted upon by the staff.

**What role should business ethics play?:**

Whether business ethics takes one or other of the forms outlined above, there is uncertainty about the role business ethics should take in improving standards of Australian corporate conduct. At times it appears to be pushed as a panacea for Australia's economic woes - to the exclusion, deliberate or otherwise, of other forms of remedy, especially legal and organisational ones. Such an approach is particularly likely from those who favour one of the first four answers to our first question.

We believe that such an approach is bound to fail. The common and legitimate complaint against such a 'stand-alone' business ethics is that it only creates a knaves' charter. Ethical standards only restrict the conduct of business people who are already ethical. They impose no effective constraints on the unethical business people who are at the root of the problem. Like an air conditioning system which operates perfectly on mildly warm days, but breaks down on the first day of a heatwave, ethical standards only work when they are not really required.

This is not to say that law provides a solution by itself. If we pass laws, we

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<sup>11</sup> Held in Brisbane, November 11-12, 1991.

hear the justified lament that the mere passage of law cannot produce behavioural change. Laws in conflict with the mores and practices of those on whom they are imposed will prove largely unworkable as business seeks to avoid or even evade their impact. Legal sanctions only work well if they are supported by congruent internalised values. Thus it is commonly argued, ethical standard setting and legal regulation must be mutually supportive.

However, even the best combination of laws and ethical standards will be defeated by an institutional environment which is not conducive to legal and ethical compliance. For example, spreading rumours about a run on a rival deposit-taking institution might contravene laws of banking and commercial libel, and be considered terribly unethical, but if a bank rewarded its branch managers solely on the basis of new accounts and deposits taken, those managers are under a massive, institutionally structured, temptation to spread such rumours.

It is for these reasons that this paper argues that the solution to improving the standards of corporate conduct lies in a combination of legal regulation, ethical standard setting, and institutional design. It is essential to approach these considerations simultaneously. Each one is insufficient, leading to failure and despairing resignation when attempted by itself. The three must be tackled in a co-ordinated way.

### **Justification:**

Having said this, the key question is how the three can indeed be co-ordinated. For us, there is a clear answer to this question, and to similar questions about the other institutions that have come into question in the nineties. That answer lies in looking at the *justification* of the relevant institution or professional activity<sup>12</sup> - a justification that must rely on the ends and values the institution should serve.

These values justify the institution under consideration. This justification provides a positive guide as to what the institution should aim for and achieve, rather than merely advising as to what it should avoid. First, those justifying values provide the basis and purpose for the legislation and regulations that govern that institution's creation, existence and conduct. In so doing it provides a basis for the purposive interpretation of that regulation. Secondly, those values provide the positive guide that should be at the centre of ethics. It sets out the positive standards which its members (employees, directors and shareholders) should follow and by which they should judge themselves and be judged by their peers. Finally, these values set out a basis for evaluating the structure of the institution in that they set standards for the criticism and

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<sup>12</sup> The general thrust of the argument owes much to Dworkin's arguments about the necessity for judges to justify the institutions of which they are a part (Dworkin, R., 'Hard Cases' in *Taking Rights Seriously*, London, Duckworth, 1977 and subsequent work) - although there are many points at which we would take issue (for example, see Sampford, C., *The Disorder of Law*, Ch 4, Oxford, Blackwell, 1989).



reform of institutions.<sup>13</sup>

There is no shortage of purported justifications for the institutions of Australian business. They are based on the benefits that the institution is claimed to provide for the members of the society of which they are a part in terms of greater national wealth, social mobility and individual autonomy enjoyed in societies with such institutions. However, this way of looking at institutions places these justifications at centre stage. They should be more than mere sop to the individuals and minorities who benefit from those institutions or the defences they raise in the political battles over their institutions. They should constitute the *raison d'etre* of the institution and should structure our thinking about them.

*Competing justifications:*

Of course it is to be expected that there will be competing justifications for many institutions and that all will be subject to dispute. Some will seek to justify corporations on the basis that they enrich their shareholders. Others will argue that corporations are only justified if they do more than increase national wealth and simultaneously provide a decent life for the people who work for them. However these competing, contested and conflicting justifications should be central to debates over the legal status, legal rights and immunities, ethics and institutional design of those institutions. Those who adhere to one or other of the justifications should act consistently with their adopted justification in adjudicating them, legislating for them or acting for or within them.<sup>14</sup> Where individuals honestly conclude that the institution is not justified as it stands, it provides them with a reason to attempt to dismantle it, change it into something that can be justified,<sup>15</sup> or failing that, restrict or nullify its operation.

The existence of competing justifications makes the co-ordination of law, ethics and institutional design more difficult. However, it encourages the development of a critical morality of business among those who are engaged in it - with all the benefits outlined above.

*Benefits for members and the wider public:*

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<sup>13</sup> It is important that this justification is seen as prior to all three. We are not suggesting that an ethicist take the values that lie behind the ethical standards which he or she would have business adopt and change law and organisational theory to suit. Neither are we suggesting that we look to the values behind the Trade Practices Act and insist that they provide the basis for business ethics. We are suggesting that we go behind all three and look to what ends the institutions should serve and then try to mould all three to make those ends more, rather than less, likely.

<sup>14</sup> This does not prevent the manufacture of purported justifications for institutions - indeed it will stimulate them. However, the citing of a justification always raises the question of its adequacy and it is always harder to defend an institution on the basis of principle than on the unquestioning assumption that it is a natural, inevitable part of the society.

<sup>15</sup> As justifications tend to be of what the institution could be rather than is, this will be particularly common.

Some of the competing justifications will centre on the financial and participatory benefits that an institution provides for its members (whether narrowly or broadly defined). Others will centre on the benefits to the broader society. Strictly speaking, the justification should not be solely in terms of the benefits to members. It is the real possibility that institutions may benefit their members at the expense of their fellows that the justification requirement was stipulated. However, the benefits enjoyed by members of the institution are highly relevant in three ways.

Firstly, where it is possible for most citizens to enjoy the benefit of membership then the existence of institutions that provide those benefits constitutes a powerful justification for granting them the privilege.

Secondly, the two are related. Institutions which generate feelings of solidarity, loyalty and commitment are generally far more effective; and the external effectiveness of institutions is one of the things which helps generate that solidarity.

Thirdly, many of the benefits to the wider community are indirect ones. Many government institutions are established to produce direct benefits - through the provision of payments or services to the public. According to neo-classical economic theory, commercial corporations provide a benefit by providing goods or services to the public at or below the price the public are prepared to pay. However, many of the most important effects of institutions are indirect. The important claim made about commercial corporations competing in the market is that they maximise the wealth of nations because of the efficiencies forced upon them by that competition and make possible better pay and conditions and more real autonomy and freedom for those who work there. Yet they are not set up with the intention of producing those benefits, indeed if they were it is highly likely that those benefits would not be realised. A commercial corporation would not survive long if it were set up with the sole aim of transferring wealth to the community or to pay high wages to its employees.<sup>16</sup> The indirect benefits are achieved (if at all) by the fact that if we have institutions of a certain kind the desired effects are more likely to occur - when business people attempt to set up institutions that maximise profits the indirect effects are to increase GDP and job satisfaction.<sup>17</sup> This is not to say that the structure of corporations and universities will necessarily lead to the claimed external benefits<sup>18</sup> and that those structures might not be set with an eye to ensuring that these benefits are likely to be achieved and that periodic checks should not be made to ensure that they have been. It is

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16 As has been demonstrated by those corporations which appear to have been established and run in order to channel wealth to their entrepreneurial owners.

17 Dr Davis McCaughey made a similar point about universities. Although universities may greatly benefit the community by providing professional training and knowledge that is commercially useful, these are, and can only be, the indirect effects of what universities are set up to do - i.e. to train people to think by means of the subjects that are best for such purposes and to pursue knowledge for the sake of it.

18 The argument is not that corporations will necessarily, or on average achieve these indirect benefits. It is that those benefits are only going to arise indirectly.

just that it must be appreciated that some results can only be achieved indirectly and that this is typical of the way that institutions can operate and be justified. Thus justifications will frequently be in the form that the institution serves its members in specified ways and that, *in so doing*, it serves broader ends.

We will now turn to consider the way that these justifying values can guide and co-ordinate legal regulation, ethical standard setting and institutional design.

**Law:**

Let us assume for the moment that the justification of commercial corporations is that they serve their members (in the broader sense of employees as well as shareholders) in ways that increase the wealth of their community by making and providing more, better or cheaper products and services. Such a justification should provide a reason for blocking off avenues by which corporations can increase their profits while decreasing wealth by tax avoidance or externalising their costs (to, for example, injured workers, future users of the environment, governments or populations<sup>19</sup>) and removing incentives for them to do so<sup>20</sup>.

These avenues may be closed off by criminal or civil sanctions, by regulation, by the requirement to seek approval possibly accompanied by an environmental impact statement, or other kinds of statements as required<sup>21</sup>.

However, the justification is also, and primarily, positive. It reminds us what the institution is there *for*. As such it justifies not only the privileges of incorporation but the powers to fulfil the function which justifies that privilege. It is on these grounds that the wide powers of boards of directors to deal with the firm's assets would have to be justified.

Such justifications offer ready-made purposes for purposive interpretations of the law governing any institution. As such it has the potential to make the law more coherent, more accessible and easier to obey (members of the institution can be reasonably certain that if they act to help the institution realise the values that justify it, then they will be within the letter and spirit of the law).

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19 We would not want to imply that this tendency to externalise costs is confined to western commercial corporations. Economic enterprises in communist countries have been among the worst polluters anywhere in the world. In our country, every Liberal health plan since 1975 has attempted to reduce the cost to government but has or would have done so by imposing extra costs on the public in excess of the government saving.

20 Note that the mere fact that the claimed benefits of institutions are indirect, does not avoid the issue. Where the action complained of directly reduces that which it is expected to enhance, the indirect benefit does need to be demonstrated in practice rather than in theory.

21 For example, tax impact statements might be required in the case of takeovers and attempts by companies to move off-shore. As the latter technically involves the takeover of a local company by a foreign entity it ought to be a proper subject for the Foreign Investment Review Board.

By such combinations of measures, law should be used to push institutions into fulfilling the purposes that justify them.

### **Ethics:**

The justification of an institution can provide the basis for the institutional and professional ethics of its members and employees. This can help indicate what individuals should refrain from doing. Thus, if the justification of a corporation is to serve its members so as to maximise the wealth of the community, the ethical business person rules out takeovers and off-shore plays that enrich either the corporation or herself at the expense of the wider community.

However, the most important role of ethics is more constructive, telling us how we should live our lives or, in some forms of institutional or professional ethics, how we should act within particular roles. For example, the core of medical ethics is to be found in professional goals like the promotion of health, the relief of suffering, and the curing of disease rather than the punishable transgressions which reflect the more serious deviations from those goals. Likewise, the justification of an institution not only provides a point for the institution, but also for activity within it. It can suggest the goals members should set themselves and how they should exercise the powers they have by virtue of that membership. It sets out the positive achievements by which members should be judged by their peers and should judge themselves - the building of an institution that can realise its potential of serving its members and increasing the wealth of the community by making and providing more, better or cheaper products and services.

Ethics such as these can, in turn, support laws that are based around publicly acknowledged values.

### **'Institutional Design':**

The provision of a justification for an institution provides a standard for criticism of the design and performance of institutions. It constantly raises the question of what structure, what design, what kinds of relationships between members of an organisation are likely to aid the institution achieving the values that justify its privilege of incorporation. (It also raises the negative question of how we can prevent some of the aberrations that prevent it achieving those values. However, as with law and ethics, the primary emphasis is on what they can positively achieve.)

Thus we should be asking what sort of institutional structure is more likely to allow corporations to produce world class goods and services that improve our exports and national wealth in a way that enhances the freedom, autonomy and welfare of its citizens. In other words, what structure will allow Australian corporations to fulfil the claims made for capitalist enterprise?<sup>22</sup>

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<sup>22</sup> In the same way as we should consider what structure allows universities to produce world class teaching and research and what structure allows the courts to

This is not an area where either author possesses any formal training. However, it does appear that some of the most successful corporations have structures that are designed to engender commitment and harness the energies and skills of members in building them into successful commercial enterprises that support their members and enrich their communities. This is especially the case in the knowledge based industries (such as computers, law, advertising, marketing and, to a diminishing extent, in universities<sup>23</sup>) but is also true to a lesser extent in manufacturing. Employees of these institutions are given more autonomy, responsibility and say in what they do individually and an increasing share in deciding what is done collectively through work groups, quality circles and even worker participation on the supervisory board of German companies. There are even isolated moves towards a more thorough-going democratisation of the workplace<sup>24</sup> supported by some academics.<sup>25</sup> The technological explosion is speeding up all these trends and unsurprisingly they are more marked in the successful knowledge based industries such as advertising and law. There, it is usual for clients to be serviced by individuals or ad-hoc groups of employees selected on the basis of shared interest and expertise rather than a permanent or rigid hierarchy. This is carried much further in the oldest and most successful examples of the knowledge based institutions - universities. Indeed the most notable English and American universities display a relative lack of hierarchy<sup>26</sup> and central control<sup>27</sup> and generally leave the individual academic with a great deal of autonomy and a large say in the few collective decisions that have to be made in a university. One is led to wonder if the university may yet provide a better model for commercial corporations than commercial corporations provide for universities. Indeed if John Matthews<sup>28</sup> and Paul Hirst<sup>29</sup> are right, the trends in knowledge-based industries will mean that the most effective and efficient corporations will become more and more democratic.

If these are to be the trends in successful business corporations then there is a

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better resolve disputes that come to it?

23 Sampford has elsewhere argued that universities might provide a better model to Australian business than current Australian business might offer to universities - *supra* n 3.

24 Note that democratizing institutions might mean that administrative law remedies might be both less necessary and more acceptable, reducing their effective 'burden' on institutions so it would no longer be true that no institution could efficiently operate with the kind of regulation inherent in the new administrative law.

25 For example, Hugh Collins, 'Against Abstentionism in Labour Law', in Eekelaar J. and J.Bell, *Oxford Essays in Jurisprudence*, 3rd Series, Oxford, Clarendon Press, 1987.

26 Both Oxford and Harvard have extremely 'flat' career structures and neither have the five levels of academic appointment we have in Australia.

27 Oxford is the collegiate university *par excellence* and although Harvard has more powerful and appointed Deans, the autonomy of academics in ivy league universities is very strong.

28 *The Age of Democracy*, Melbourne, Oxford University Press, 1989.

29 *After Thatcher*, London, Macmillan, 1989.

real chance that businesses may both add to the prosperity of the community and the autonomy of their members. They are also likely to be the kind of business organisations in which 'ethical circles' could most easily and meaningfully flourish.

### **Why should business corporations have to justify themselves?:**

For many, the idea that business should justify itself is likely to be resisted, even resented. Some might point to the failures of Eastern bloc countries and assume that the discrediting of the most publicized alternative obviates the necessity for justifying their own. Some might see justification as beside the point. They would say that they are 'just doing business' as if to say that 'being in business means never having to say you are sorry'<sup>30</sup> - or perhaps 'never having to mean it when you do'.

However, there are at least three reasons why we should insist on such justification.

First, we would agree with John Rawls' insistence that justice is the first virtue of institutions, but taking the next step and adding that that should be true of non-government as well as government institutions.

Secondly, we should not be complacent about the failure of Eastern bloc socialism. We have had our own share of institutional failures in which institutions failed to live up to their justifications and ended up serving only the interests of those who ran them.

The institutions of the command economy were justified on the basis that they would produce a revolution that would end scarcity, domination and the need for law. Instead those institutions were run for the benefit of the apparatchiks who dominated them and took rather than gave to society. In the end they collapsed from within as much as they were torn down by those in the host society who resented apparatchiks' parasitic and conspicuous (relative to their society) consumption.

The entrepreneurial companies were justified as institutions which would improve the performance of companies that manufactured goods and produced services to the benefit of shareholders and the public at large. Instead they were run for the benefit of a few who took from, rather than gave to, the rest of society. At first this was at the expense of the wider public via the reductions in tax they generated and, sometimes, the higher prices they charged. Later this was at the expense of the shareholders and depositors whose investments were often plundered to keep the entrepreneur afloat. The entrepreneurial companies collapsed from within and have since been rounded on by those outraged at the conspicuous consumption of the entrepreneurs.

Thus the institutional disasters of the East and West can be seen as the failures of institutions supposedly central to the organisation of those societies. They show the dangers of too easily assuming that institutions will work for the

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30 With apologies to 'Love Story', 'Wall Street', or, quite possibly, both.

public good. Some 'vulgar' Marxists thought that this was a necessary corollary of putting institutions under the control of Marxists. Some 'vulgar'<sup>31</sup> capitalists assumed that 'private' institutions freed of government control would operate like selfish individuals and thus, according to their theory, serve the public good.

We need to take our institutions and the problems of achieving goals through them more seriously. We need to ask what institutional law, what institutional ethics, and what institutional design will allow our institutions to justify themselves by fulfilling the purposes we set for them in the late twentieth century.

In asking these questions we should not look to the Eastern bloc for what to avoid but at other Western countries where corporations have been better able to fulfil the justifications of corporate capitalism. At the very least it is necessary for Australian business to justify why it should continue to operate as it does rather than follow the more successful modern success stories in Western Europe and Japan. This is particularly important in the light of Australia's greatest economic tragedy - the way we blew our post-war chance of becoming one of the economic power-houses of East Asia. Consider Australia's position at the end of the second world war - a well-educated workforce; rapid expansion of industry during the war; justified national pride and high morale; massive natural resources; and excellent record in basic research, providing it with the knowledge-base to become world-leaders in selected areas of high-technology; and perhaps most importantly, an immense geographical advantage in being located in the region that was to post the most phenomenal sustained growth in human history, with its potential rivals either in ruins from the war, or agricultural backwaters still waiting for their industrial transformations to occur. Less than fifty years later, far from being the power-house of East Asia, we are weaker than ever. Australian business must accept responsibility for this decline and should not try to lay all the blame on government. Most of the relevant decisions on investment (and research and development) were made by the managers and directors of public companies and the institutions that financed them.

The third reason why we should insist that institutions must justify themselves is the concentration of power and resources represented by the modern corporation. This threat has long been appreciated by socialists and civil libertarians. However, it should be appreciated by neo-classical economists as well. Corporations are economic combinations of investors and neo-classical economists should be as wary of them as they are of combinations of traders and trade unionists. Adam Smith is the most frequently quoted on this point when he said that rarely do merchants gather together that a conspiracy against the public interest does not result. Fifty years after he issued that warning, incorporation was made easy and limited liability permitted for good reason. But we should never forget the privilege of incorporation and the benefits of limited liability and ensure that those privileges granted and risk taken in

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<sup>31</sup> See Sampford, C., 'Dworkin's Claim to a Socialist Inheritance' (1991) 16 *Bulletin of the Australian Society of Legal Philosophy*, no.56, 37.

permitting concentrations of economic power do serve wider purposes than the aggrandisement of those who head these organisations.

Despite the likelihood of resistance and resentment that some in business would feel at having to justify their activity, few would not claim that this society is justified in leaving the bulk of economic activity in the hands of non-government corporations. Most would insist that the society derives great benefits from it. The tripartite solution insists that business ethics, business regulation and corporate structures are such that those benefits accrue, thereby justifying the society's faith in such organisations and justifying business for accepting the power and privilege that follows from it.

### **Different emphases:**

Looking to the justification of business has two important consequences for business ethics. First it emphasises those things which business ought to do rather than those things it should not do. Secondly it sees ethics as something for the corporation, for the business enterprise rather than for the isolated individual. We will briefly deal with each.

#### *An emphasis on positive rather than negative ethics:*

Ethics is seen as what business should seek to achieve rather than what it should avoid. If the only issue were to avoid the evil that business may do the answer would be simple - get rid of business. This is what anarchists of left and right suggest should be done to government and some revolutionary socialists would do with business. The answer to both is to look to the justification of each and to structure the relevant ethics, law and institutional structure around that justification. This does not rule out substantial challenges to one or both - or even their destruction (if they cannot be justified against the alternatives). But if that conclusion is not reached this approach does suggest that the positive values by which business may be justified should provide the key to our thinking about them.

This concentration on positive prescription does not exclude a consideration of negative proscriptions. On the contrary, the latter should be seen as deriving from the former. Thus if the justification of the kind of business we have is that it improves national wealth and provides for greater autonomy for individuals, then enriching an entrepreneur at the expense of shareholders or enriching the company at the expense of Australia is not merely a breach of rules against bad corporate behaviour, it is contrary to the whole reason for having, and being in, business. It is not doing business in an unethical way, in a fundamental sense it is not doing business according to the model of business proclaimed and justified by its proponents.

Similarly, we would argue, if capitalist business is supposed to increase individual autonomy and choice then dehumanisation of work, de-skilling of labour and savage reductions in wages and conditions are not only unethical goals for Australian business but should be seen as a failure to do business according to the terms in which it is justified.

Thus very strong negative proscriptions can be derived from the positive



justifications of business ethics so conceived. Furthermore, this manner of derivation militates against a legalistic avoidance of those obligations. Where there is a negative proscription, it is possible to engage in long and indecisive debate about whether an action complained of falls just within, or just without, the prescription. The dividing line between conduct in breach and conduct not in breach is often impossible to determine with any precision and has to be the subject of exhaustive argument. But where ethical action is prescribed in positive terms, these arguments dissolve - because actions on both sides of the dividing line inhibit rather than promote those values by which the institution is justified.

*An emphasis on institutional rather than individual ethical concerns:*

Although we do not have the time to develop the point here, it should be noted that the approach we are taking departs from the common tendency to see ethical problems in essentially individual terms. This is a tendency emphasised by the return of highly individualistic ideologies during the 1980s where economies and societies are understood in terms of the actions of individuals. As argued elsewhere, this approach either ignores non-government institutions or distorts them by seeing them as either acting like lone individuals or as made up entirely of contracts between lone individuals.<sup>32</sup> Such approaches fail to take institutions seriously. The approach suggested here does take corporations seriously and seeks both an analysis of the problems - and the basis of the solution - in terms of the institutions of business.

In so doing we hope not only that Australian business ethics will have a future but that Australian business will too.

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32 *Supra n 3.*